



MEMO

To: Board of Directors
From: Company Secretary
Subject: **SHAREHOLDERS DIRECTION RE ANNUAL ACCOUNTS**

We have received a 'direction' from our largest shareholder requesting that we prepare and have audited the company's 30 June financial statements. They have stated that they need the information to assist them in preparing an information memorandum for a fund raising for the group.

To assist in your understanding of what the process is following this 'request' I set out below some pertinent information, some of which may be considered unnecessary at this time but I include it for the sake of completeness.

Obligation to Keep Financial Records

Notwithstanding that it is now several months after the 30 June close-off, I confirm that the financial records are adequate to provide the information necessary to respond to this request.

Pursuant to section 286 of the Corporations Act all companies – from the largest stock exchange listed multi-national down to the smallest private company – must keep adequate written records of all accounting/financial transactions sufficient to enable them to compile financial statements if required.

Specifically, under sec.286(1) the financial records must be such that:

- (a) correctly record and explain its transactions and financial position and performance;
and
- (b) would enable true and fair financial statements to be prepared and audited.

All companies must also retain financial records for at least 7 years (after the end of each financial year) – sec.286(2).

Any contravention of sec.286 a *strict liability* offence, which essentially means it is not necessary to prove intention, knowledge, recklessness or negligence (see Section 6.1 of Criminal Code).

'Financial records' are defined in sec.9 to include:



- (a) invoices, receipts, orders for the payment of money, bills of exchange, cheques, promissory notes and vouchers; and
- (b) documents of prime entry; and
- (c) working papers and other documents needed to explain:
 - (i) the methods by which financial statements are made up; and
 - (ii) adjustments to be made in preparing financial statements.

In addition to these statutory obligations, it is essential business practice to prepare accounts regularly – as we do – so that the directors are aware of how the company is trading and performing financially, whether there are pending funding needs, etc. Also, we need financial information for various other reasons such as to prepare tax returns and provide lenders with reports.

Statutory Requirement to Prepare Accounts

Sec.292 requires only the following entities to prepare annual financial and directors' reports and have them audited:

- public companies
- disclosing entities (unlisted and Australian stock exchange listed)
- large proprietary companies
- most foreign-controlled small proprietary companies.

Small Proprietary Company

However, we are a small proprietary company – i.e., a company which is not a 'large proprietary company' – as we satisfy 2 of the 3 criteria set out in sec.45A(2); these are:

- (a) the consolidated gross operating revenue for the financial year of the company and the entities it controls (if any) is less than \$25 million;
- (b) the value of the consolidated gross assets at the end of the financial year of the company and the entities it controls (if any) is less than \$12.5 million;
- (c) the company and the entities it controls (if any) have fewer than 50 employees at the end of the financial year.

Therefore, we do not have any financial accounts and/or reporting obligations except as provided for in sec.292(2); that is, if directed to do so under sec.293 (shareholder direction) or sec.294 (ASIC direction).

Shareholder Direction

Sec. 293 provides that shareholders controlling at least 5% of a company may direct that accounts (financial statements and reports) be prepared and sent to all shareholders (ie, they cannot be given just to the requesting shareholder/s).



The direction must be signed by the requisitioning shareholders and given no more than 12 months after the end of the company's financial year. Also, it may specify all or any of the following:

- that the financial report does/does not have to comply with some/all accounting standards
- a directors' report, or only part thereof, need/need not be prepared
- the accounts must be/need not be audited.

Accounts prepared pursuant to shareholder direction are not lodged with ASIC.

Summary

In my opinion we have no option but to comply with our shareholder's request as the Corporations Act allows them to given this 'direction' and they have acted strictly in accordance with the Act.

There does not appear to be a time frame stated in the Act by which the company must comply with the direction, and no specific date has been stated in the shareholder's request, but in sec.294 (re ASIC direction) it says that the deadline "must be a reasonable one in view of the nature of the direction" – so I guess that applies to us too.

DISCLAIMER

The comments in this memo reflect some commercial aspects and observations on the matter experienced or observed by the writer in practice as he understands them. The information is given as a guide only and does not represent a definitive or legal view of any of the issues raised, covered or referred to and the reader is urged to seek his own professional advice on all aspects of, or pertaining to, this and any related matter.